BANKING & COMMUNITY

Perspectives

FEDERAL RESERVE BANK OF DALLAS SECOND QUARTER 1997

The Power To Move

Public/Private Partnership Allows Auto Shop Owner to Expand

Sengchanh "Sam" Khamphoumanivong, owner of Sam's Auto Repair, and Bill Doeppenschmidt, a vice president at CaminoReal Bank, stand in front of the expanded business.

The once-empty building is humming with business again. The former service station about 10 miles east of downtown San Antonio had been sitting idle for about a year. It was just what Sengchanh "Sam" Khamphoumanivong needed to expand his auto repair business.

Since its opening in 1993, Sam's Auto Repair had been located in a cramped, one-car garage without an automotive lift. Khamphoumanivong and his employees had to work outside because of limited space, even during bad weather. The old garage lot he was renting wasn't paved. His new location and buildings would attract new customers and allow him to work year-round, regardless of the weather. And after working in the auto repair field for more than 12 years, Khamphoumanivong would truly be able to grow his business.

Thanks to a public/private partnership involving CaminoReal Bank, three San Antonio-area organizations that assist small businesses and a lot of hard work from Khamphoumanivong, Sam's Auto Repair opened at its new site in April 1996. A loan package worth $200,250 allowed Khamphoumanivong to buy the closed service station, which has a three-bay shop, a three-bay garage with lifts, and a service station with a small office and convenience store.

"The loan has improved my business a great deal," Khamphoumanivong said. "The new location has better access, and having a paved lot is a big improvement. I have a lot more business now since my location is bigger. The convenience store has added business, too."

Putting the loan package together wasn't easy. It required meetings of Khamphoumanivong and representatives of CaminoReal Bank, the San Antonio Local Development Co. Inc. (SALDC), the San Antonio Business Development

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Public & Private Partnership

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Fund (SABDF) and the local Small Business Development Center (SBDC).

"Sam had a great idea when he approached us about buying the location, but he needed help to get it done," said Bill Doeppenschmidt, a vice president at CaminoReal Bank. "You've got to put a lot of effort into these types of loans. They don't happen overnight. But when it works out, it's a good way to put a good loan on the books."

The loan package Khamphoumanivong received to expand his auto repair business has helped bring in new customers. Additional income comes from the convenience store.

Khamphoumanivong had been a customer of CaminoReal Bank for several years with a business checking account. When Doeppenschmidt started working with Khamphoumanivong in October 1995 on the loan package, Khamphoumanivong did not have equity capital, working capital or a business plan, which made it difficult for him to qualify for traditional bank financing.

Doeppenschmidt referred Khamphoumanivong to the local Small Business Development Center for assistance with a business plan and projections.

Doeppenschmidt then brought together representatives of the loan funds and the development center, and the property seller and Khamphoumanivong. With the bank as the convener, a deal was struck.

CaminoReal Bank gave Khamphoumanivong a $97,500 loan with a 15-year amortization to purchase and improve the property. The loan has a five-year term, after which the borrower's credit and the loan rate are reevaluated. CaminoReal Bank has a first lien on the property.

San Antonio Local Development Co., which administers the Economic Development Administration's revolving loan fund, facilitated a $68,000 loan to Khamphoumanivong and holds a second lien. The fund offers below-market, fixed-rate financing for up to 33 percent of project cost.

The San Antonio Business Development Fund, a multibank community development corporation, participated in the financing package with a $25,000 loan to Khamphoumanivong and holds a third lien. This development fund was created by a consortium of banks and the city of San Antonio to provide equity and debt financing to small emerging companies, with an emphasis on minority- and women-owned businesses.

SABDF President Gilbert Gonzalez said his agency knew it would be a tough deal to put together but that it could be structured so all the players would be comfortable with the loan. Gonzalez said concerns about collateral

Small business loans can make it possible to add jobs in a community. Sam's Auto Repair now employs 10 people.

were put aside, and the loan was based on Khamphoumanivong's character and repayment history.

"We saw a lot of potential in Sam's business," said Mike Mendoza, a senior loan officer for San Antonio Local Development Co., which is part of the city of San Antonio's economic development department. "The San Antonio Business Development Fund loan also enhanced Khamphoumanivong's position and made it easier to get our part of the loan package approved by our board. As a development agency, we are maximizing the use of federal funds by participating with a private bank and a community development bank. That's a good use of federal dollars."

With approximately $260 million in total assets, about 10 percent of CaminoReal Bank's portfolio consists of small business loans. Doeppenschmidt said his bank is committed to small businesses, and working with area development agencies makes good business sense.

“Participating in these programs allows us to make a loan to a company or an individual to expand a business that normally we couldn’t do as a conventional loan,” Doeppenschmidt said. “You can add jobs, sometimes add beauty to a community and keep a small business operating. And that makes this country go round.”

Khamphoumanivong said his new location on a main street offers greater visibility. He employs a total of 10 people, including his sister, father, brother and sister-in-law. Clear goals and lots of long hours have been a key part of his success, he said.

“The biggest improvement was the location. The old shop had a gravel drive. My customers would drive their Mercedes and BMWs to me and get them dirty. They thought I was a good mechanic but didn’t like the location,” Khamphoumanivong said.

He plans on adding gasoline sales this year, as part of his business plan. He also has been expanding his customer base with commercial fleet contracts and with the neighborhood residents who shop at the convenience store.

Doeppenschmidt encourages banks and development agencies to form long-term working relationships to overcome potential roadblocks.

“The biggest problem is there are so many programs out there that we don’t know about. Education of lending officers at banks is important,” Doeppenschmidt said. “You’ve got to go the extra mile. Every loan that comes in your front door might not be able to work on face value. But if you use these business development groups and the funds that are out there, you can make these things work.”

Fast Facts

Sam’s Auto Repair

Sam’s Auto Repair had the opportunity to expand from a one-car garage to a six-bay garage and convenience store because of a public/private partnership. The total development package was $200,250, of which $175,000 was used to purchase the land and improvements, $20,000 was used for working capital and the balance of $5,250 covered closing costs. All the loans have five-year terms after which time they can be paid in full or possibly can be rolled into one loan with CaminoReal Bank.

CaminoReal Bank, $97,500
Fifteen-year amortization with a five-year term at *Wall Street Journal* prime rate plus 2 percent (10.5 percent) and a first lien position

San Antonio Local Development Co. Inc., $68,000
Economic Development Administration revolving loan fund
Fifteen-year amortization with a five-year term at 8 percent and a second lien position

San Antonio Business Development Fund, $25,000
Multibank community development corporation
Ten-year amortization with a five-year term at 13 percent and a third lien position

Owner Equity, $9,750

Total — $200,250

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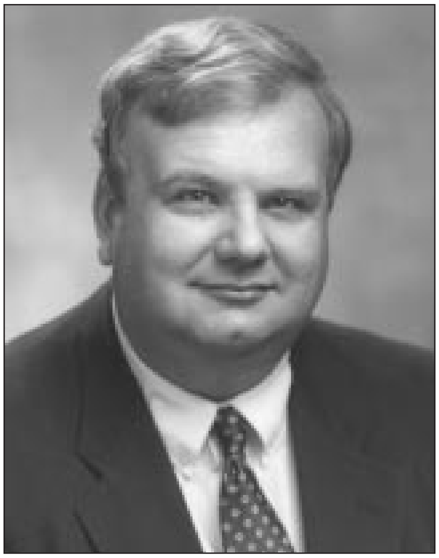
Commentary

The Numbers Show Improvement In Lending

Lawrence B. Lindsey resigned from the Federal Reserve Board of Governors in February and has joined the American Enterprise Institute in Washington, D.C., and a New York economic advisory firm. Drawing on his experience as chairman of the Fed's oversight committee on consumer and community affairs, he is planning a book about community development, tentatively titled Beyond Abuse and Neglect. *The following remarks were excerpted from a speech he gave at the Federal Reserve Bank of Dallas' community development lending conference in October 1996.*



Lawrence B. Lindsey—
former member of the Federal Reserve Board of Governors

> The numbers show that we have reached a point where race- or ethnic-based discrepencies seem to have largely disappeared

Access to credit by individuals and communities that are the target of our economic development efforts has reached unprecedented levels.

The data for 1995 indicate that in a year when the number of conventional home purchase loans decreased overall from 1994, lending to African-Americans, Hispanics and Native Americans went up. The 1995 figures are part of a four-year trend reflecting a steady upswing in mortgages granted to these groups, including significant double-digit increases during 1992-94.

The numbers show that we have reached a point where race- or ethnic-based discrepancies seem to have largely disappeared. For example, if the market for conventional, non-government-assisted loans is defined as families who earned $50,000 or more in 1994, then the proportion of such families getting mortgages in 1995 was 9.6 percent for whites, 8 percent for blacks and 11.6 percent for Hispanics.

Including all mortgages, conventional and government-assisted, and dropping the income threshold to $25,000 shows that 6.4 percent of whites, 6 percent of blacks and 7.2 percent of Hispanics got mortgages in 1995. Confining the base to married families with children—those most likely to be in the market—produces an even more compelling case that disparities have largely disappeared.

The Federal Reserve's Survey of Consumer Finances gives good reason to believe that the penetration of underserved markets in the credit card business was as dramatic and preceded the large-scale increases in mortgage credit.

Surveys conducted in 1989 and 1992 showed the proportion of white families with outstanding credit card debt rose only slightly—from 42.5 percent in 1989 to 44.1 percent in 1992. In 1995, this proportion was 47.5 percent. But the growth in credit card use as a source of finance among nonwhites was substantial. The proportion of nonwhite families with outstanding credit card balances rose from 34.1 percent in 1989 to 42.9 percent in 1992 and to 48.8 percent in 1995. This suggests that a potentially debilitating economic burden has been lifted from a significant share of the population, who can now meet economic emergencies and time their purchases with greater ease.

Why has all of this occurred just now? A part of me would like to conclude that this is the result of a permanent change in attitudes in America. While I certainly believe that we are a more enlightened country than five or 10 or 20 years ago—that our collective consciousness has been raised, if you will—I do not believe this is the whole story.

In the short term, one can rely on a sense of guilt or charity or a fear of enforcement action to motivate behavior. But it will not last. The only permanent motivating force in this world is self-interest. Without question, the most important economic development has been a decline in the underlying rate of inflation and the consequent decline in medium- and long-term interest rates.

But the reduction in inflation…
has done more for home ownership
opportunities among low- and
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by the government

Let's do the standard math involved in any home financing decision. In 1990, fixed 30-year mortgage rates averaged 10 percent. Recently, they have been around 8 percent. The principal and interest payments on a $100,000 mortgage declined from $878 to $734. Using a standard set of assumptions regarding property tax and insurance payments (PITI) and a PITI-to-income ratio of 28 percent, the annual qualifying income for this mortgage has fallen from $48,771 to $42,600. That $6,171 decline in qualifying income comes at a very dense part of the income distribution, particularly in the minority population.

And when one considers mortgage market innovations that have eased traditional underwriting constraints, the increased opportunity resulting from lower inflation and lower long-term rates is even more amplified.

There is a school of thought among some politicians that fighting inflation is bad for low- and moderate-income people. But the reduction in inflation during the 1980s, and the continuation of that policy during the 1990s, has done more for home ownership opportunities among low- and moderate-income groups than any program administered by the government.

Our system of long-term fixed-interest rates and the home mortgage interest deduction makes increasing inflation highly profitable to those who already have financed their homes. That is why we all grew up being taught that homes are a great inflation hedge.

If, however, you are simply in the market for physical shelter, and not a tax shelter or inflation shelter, high inflation—and the resulting higher long-term interest rates—prices you out of qualifying for a home. Furthermore, if your income is fairly moderate, you may not even qualify for the home mortgage interest deduction. Thus, a low-inflation environment is a key to maintaining home ownership opportunities.

A Different Kind of Club

Recognizing that an educated borrower can become a good banking customer and a solid neighbor, nonprofit groups and banks are working together to launch a different kind of club: the home-buying club.

These clubs provide in-depth education and resource options for potential borrowers, as well as a realistic look at all the steps involved in buying a home. Clubs sponsored by nonprofit groups may work with members for a year or more, focusing on long-term credit rehabilitation, household budgets and down payment savings plans to help members become bankable.

In addition to forming partnerships with nonprofit clubs, some banks have established their own clubs. Bank-launched clubs may offer their members reduced fees on savings and checking accounts and mortgage and closing fees. Some clubs even prequalify loan applicants upon successful completion of the program.

No matter how they are structured, the clubs all have one goal: an educated borrower with stable credit ready for home ownership.

Nonprofit-sponsored clubs

"Our No. 1 goal is to educate members to be able to buy homes, so they understand the process, the players involved and where they fit in," said Kimberly Bradford-Brown, business development coordinator of the NAACP Community Development Resource Center (CDRC) in Austin.

Bradford-Brown developed a one-year curriculum for the CDRC homebuyers club, which was formed in August 1996 with 11 members. Along with education, the CDRC emphasizes long-term credit rehabilitation to help each club member become bankable.

Kimberly Bradford-Brown, business development coordinator for the NAACP's Community Development Resource Center in Austin, answers a question from a member of the homebuyer's club.

"We saw so many people coming in who had credit issues, and most needed at least a year to get those cleared up," Bradford-Brown said. "The only requirement is a genuine desire to be a homeowner. They sign a contract with the club to show they will be committed to the whole one-year process. It's not a quick fix."

Club members develop individual budgets and down payment savings plans. Members must call Bradford-Brown once a week, attend monthly educational workshops and prove they are making progress with their savings plans. Workshop topics include understanding credit, maintaining household finances, planned borrowing, preparing for home ownership, housing tours of the Austin area and the steps involved in getting a mortgage. NationsBank has provided a guest instructor for the course; other guest instructors include real estate agents, city inspectors, appraisers and mortgage brokers.

"We're getting a lot of support from the banking community," Bradford-Brown said. "After the club members have completed the process, the loan officer won't have to spend time to educate them. An educated borrower is a better customer."

The San Antonio Development Agency (SADA) also helps educate potential borrowers. Nine financial institutions have teamed up with SADA to provide resources for its homebuyers club: Bank of America, Broadway Bank, Bank One, Dimensions Mortgage, Frost National Bank, Guaranty Federal Savings Bank, Mellon Mortgage, Norwest Mortgage and Texas Commerce Bank.

To get into SADA's 10-hour program, applicants must provide detailed information on income, credit and current bills. SADA runs a credit history report on each applicant as the first step in building an individual budget/savings plan and to help determine how much families can afford to spend on a home. More than 300 families have graduated from the program since it began in November 1995. Of those, 80 have applied for loans, 25 have closed on loans, and 16 are waiting for construction to start or conclude.

Although 74.2 percent of SADA participants earn incomes of 80 percent or below the San Antonio-area median, the program is open to all income levels. Guest speakers include loan officers, builders and real estate agents, who cover such topics as down payment assistance and subsidies, and floor plans of available properties. SADA tracks all participants through to their loan closings. As with the NAACP program in Austin, SADA makes a commitment to work with families no matter how long it takes.

"Our goal is to make sure participants have access to the information and to a home mortgage for which they can qualify," said Albert Uriegas, an executive assistant at SADA. "As people become better educated, they can get into home ownership aware of the responsibilities of all parties and not get into serious problems later. When families know what they can afford, they can make the financial decisions that will ensure them quality housing. Families also can explore the assistance programs available to homebuyers."

Bank-sponsored clubs

Bank-sponsored clubs often feature a variety of savings, checking and loan services, packaged into incentive plans for members once they complete the program. The Bank of America Homebuyer's Advantage Club offers discounts on bank and mortgage fees, and savings and checking accounts free of service charges for one year. The bank recognized a potentially lucrative long-term market, as well as a better way to quantify and track its marketing efforts.

"It's good business," said Bill Allin, vice president and Texas area manager with Bank of America Mortgage in Irving. "We've been doing a lot of mortgages through the club. We offer the whole package because we want an ongoing relationship. Hopefully, we can go back to them later with other products."

Bank of America's pilot club, launched in the spring of 1996, grew out of earlier seminars on home buying. Clubs are now active in the Dallas, Fort Worth, Houston, San Antonio and Austin markets.

Upon completion of the bank's buyer-education program, club members may qualify for a fixed-rate home loan with a

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From left, CRDC homebuyer's club members Cynthia Carter, Mary Bennett and Lenora McFadden listen to a presentation by retired real estate agent Mary Lee Comer at a meeting in Austin.

DID YOU KNOW...?

CRA Information on the Internet

Bank CRA examination ratings and a listing of upcoming exams are now available on the Internet. You can access the information at your convenience, via the Web sites listed below.

Web sites for CRA ratings

Federal Deposit Insurance Corp.
www.fdic.gov/banknews/monthexam.html

Federal Reserve System
www.bog.frb.fed.us/DCCA/CRA

Office of the Comptroller of the Currency
www.occ.treas.gov/cra/crasrch.htm

Office of Thrift Supervision
www.access.gpo.gov/ots/press_rel.html

Web sites for CRA examination schedules

Federal Deposit Insurance Corp.
www.fdic.gov/databank/qbp/excra.html

Federal Reserve System
www.bog.frb.fed.us/DCCA/CRA

Office of the Comptroller of the Currency
www.occ.treas.gov/cra/duecra.htm

Office of Thrift Supervision (OTS)
www.access.gpo.gov/ots/press_rel.html

A Different Kind of Club

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down payment as low as 5 percent, 2 percent of which can come from family gifts, a government agency grant or a nonprofit grant. That means some members only need to provide a 3 percent down payment.

As with the other clubs, credit rehabilitation is the biggest issue people face coming into the Bank of America club, said Jim Richardson, vice president of community development. That process can take up to one year or longer. Club meetings are scheduled for evenings and Saturdays in community centers. The setting is casual, and the bank often provides child care.

"People need to feel comfortable about discussing their financial situation," Richardson said.

Loan officers and real estate agents often attend the meetings, where the bank presents information on down payment assistance programs. The bank makes sure it follows up with members, to help them gather information and accurately complete forms, Allin said.

The bank services offered to club members become tools to encourage saving and good credit practices. A special savings account is offered with no service charge, to encourage club members to save for their down payments.

"We can offer a lot of other services along with the home loan," Richardson said. "We want not only their home mortgage business but to develop a long-term banking relationship with them."

Potential for expansion

After the NAACP's first class graduates, Bradford-Brown wants to work with Austin-area banks, real estate agents and others to generate incentive packages for club members. Homebuyer clubs are in the works at two other NAACP community development centers in the country. The NAACP plans to open more centers in 1997. Bradford-Brown hopes to see clubs at all centers eventually.

"People can live the American Dream. I tell people if you can dream it, you can live it if the commitment is there," Bradford-Brown said.

In San Antonio, the SADA program is exploring options to offer other area nonprofit groups homebuyer club services, Uriegas said.

"There's a lot of interest in getting into the classes," Uriegas said. "We're getting ready to do some expansion in outreach efforts."

Perspectives
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